

Illicit Financial Flows: Case Study of Lebanon

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Under developed
countries



Illicit Financial Flows



Weakness of Laws



Lack of Control



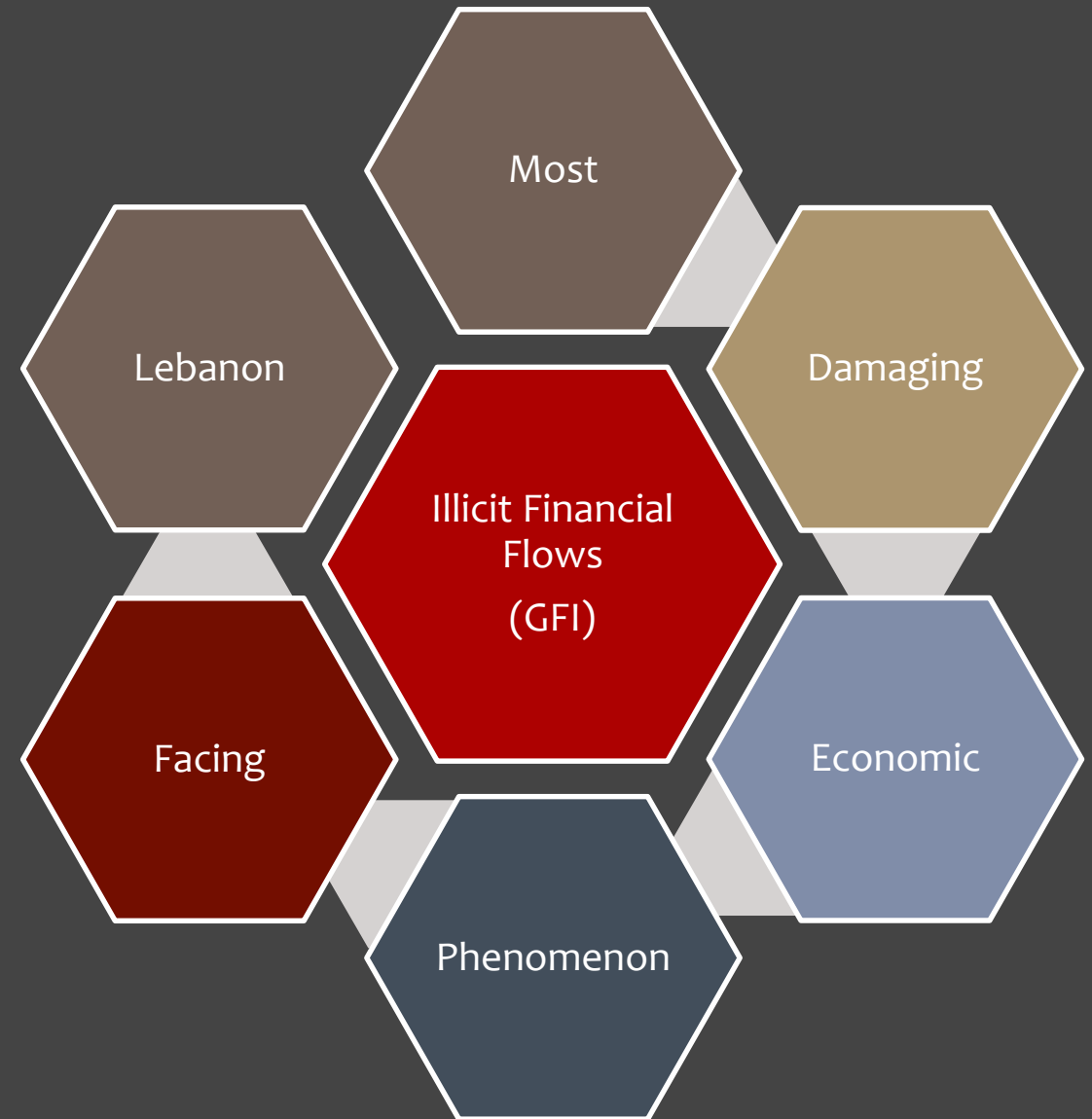
Corruption



Greed

Agenda

- Introduction
- State of Art
- Analysis
- Recommendations



Introduction

- Economic goals:
 - Efficiency: Situation in which it is impossible to generate a larger welfare total from the available resources
 - Freedom: Individuals are free to secure and protect their human resources, labor and private property
 - Growth: Increase in a country's productive capacity, as measured by comparing gross national product (GNP) in a year with the GNP in the previous year
 - Stability: Economic system of a nation that displays only minor fluctuations in output growth and exhibits a consistently low inflation rate.
 - Equity: fair distribution of wealth and income in a society (not assistantship)
- All this leads to an optimization in using the available resources

Introduction

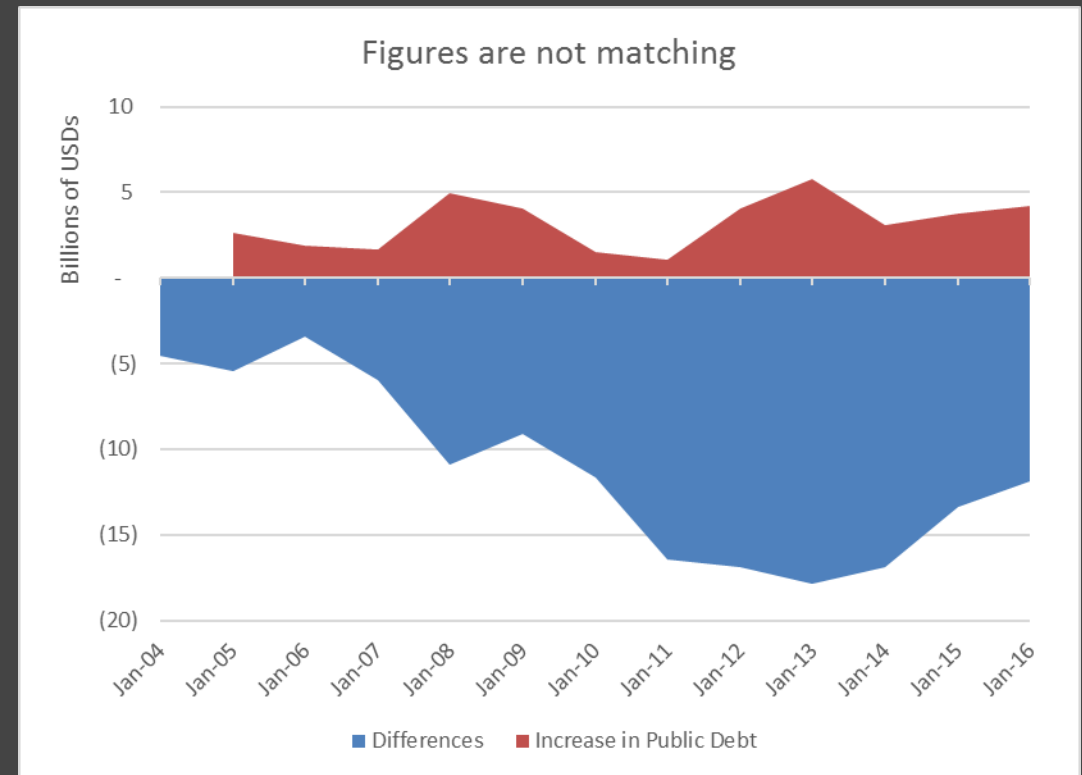
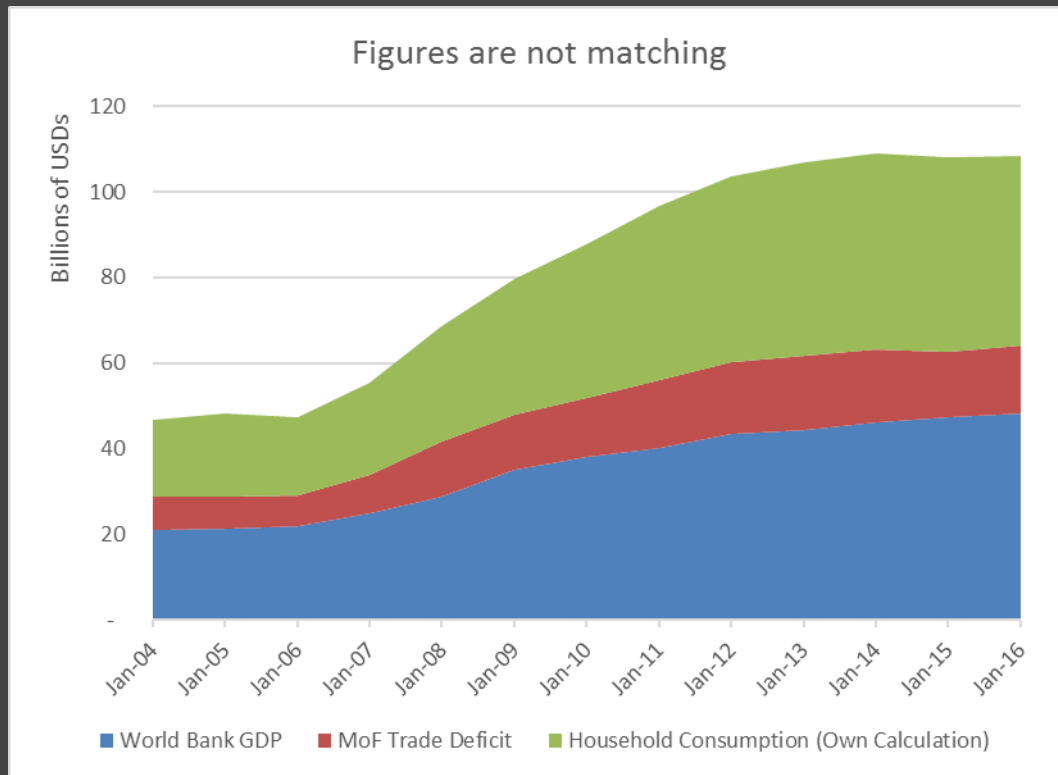
- Problem: Some resources could be out of use by mis-scheduling or by bad intention
- Illicit Financial Flows is a bad intention to monopolize financial resources for personnel enrichment against the well being of whole economy
- Developing countries are the most who suffer from the IFF
- Lebanon, is one of these countries and the size of the IFFs starts to be a major issue for the Lebanese economy
- IFF deprives Lebanon from a huge potential of investment that is crucial for the Lebanese economy

State of Art

- 3Cs: Corruption, Commerce and Crime
- Large informal sector → 36% of the Lebanese economy
- Economic indicator shows a huge lack in controlling the business transactions → legal issue, technical issue, cultural issue
- Corruption constitutes the main tool that IFFs' operators use to facilitate their mission in Lebanon
- USD 10 Billions is the cost of corruption per year for the Lebanese Government including IFFs, Tax Evasion... in addition to the cost of opportunities

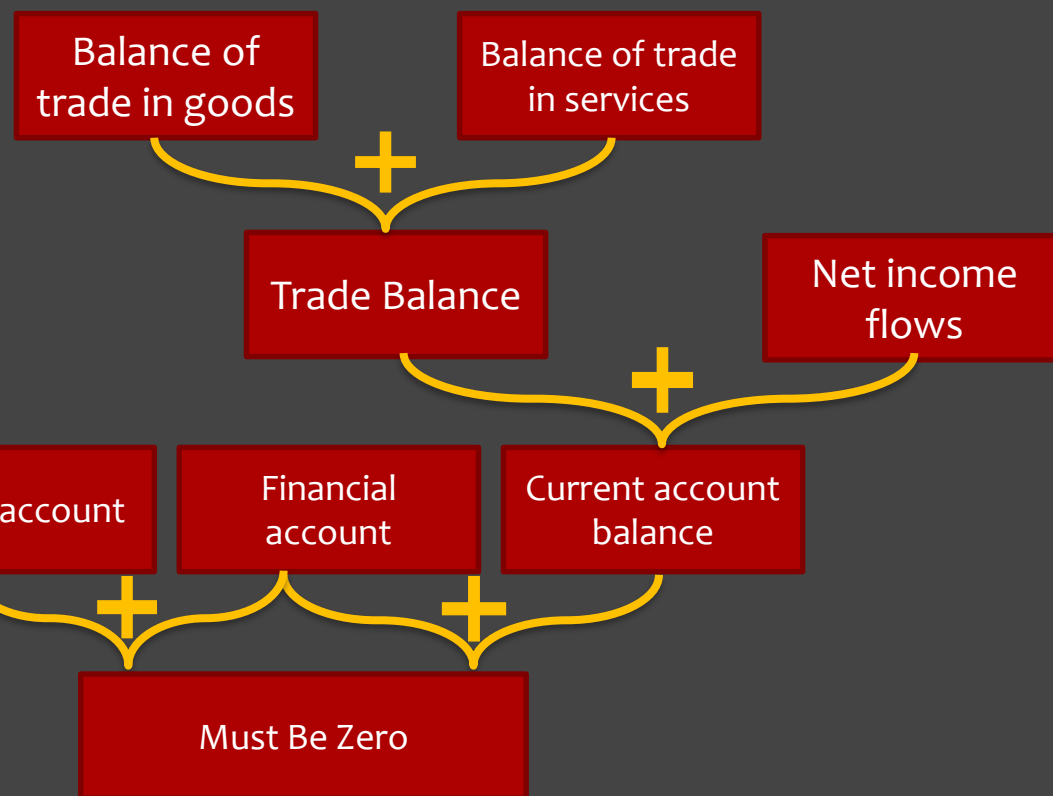
State of Art

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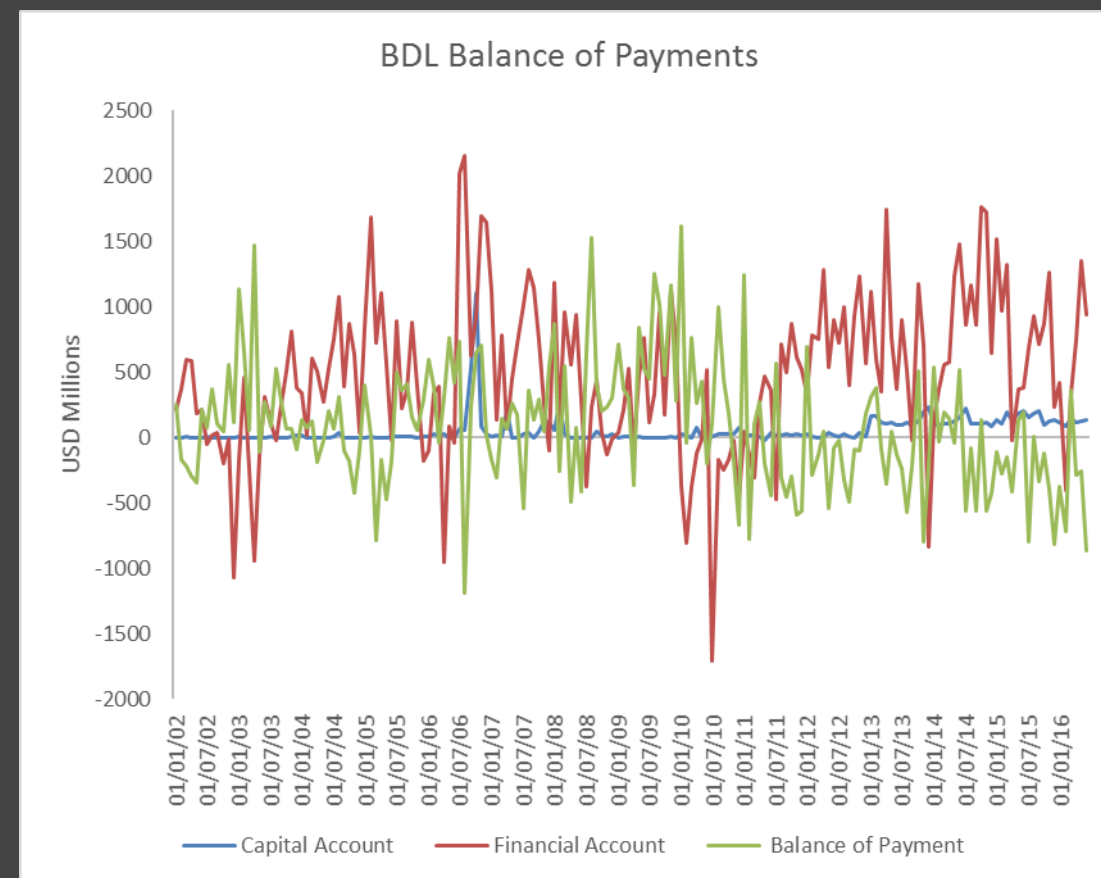


State of Art

Balance of Payments

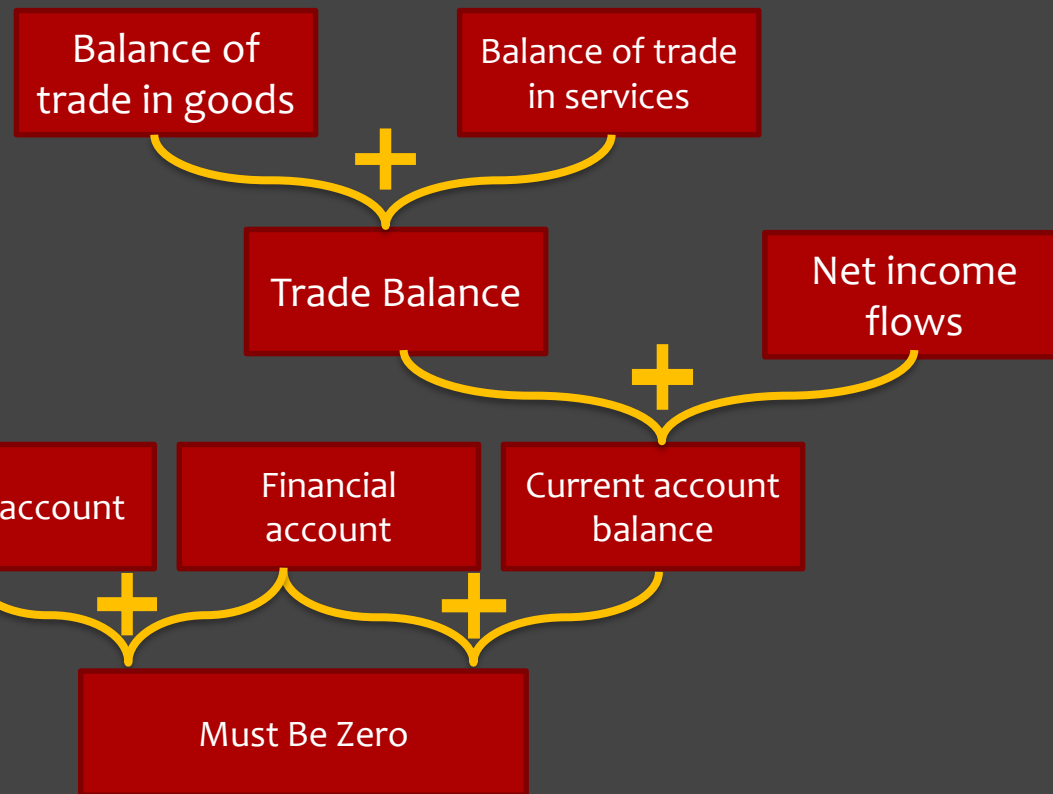


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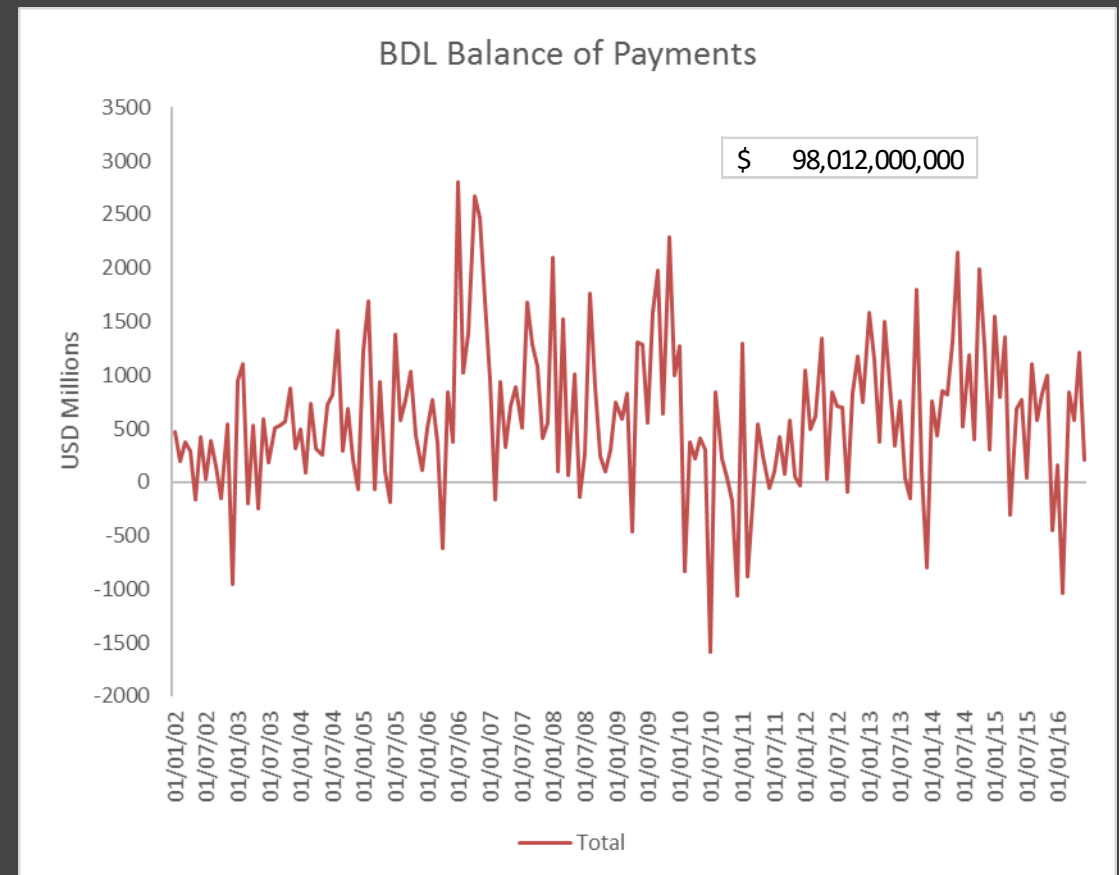


State of Art

Balance of Payments



No Matching



State of Art

- Import Under-Invoicing (Inflow)
- tax evasion
- Type of Commodities

	Export to Italy (000's USD)			Import from Italy (000's USD)		
	ITC	LB Customs	Cus-ITC	ITC	LB Customs	Cus-ITC
Apr-14	1543	1543	0	167812	166976	-836
May-14	1770	1770	0	156952	155920	-1032
Jun-14	2180	2180	0	164754	164333	-421
Jul-14	5468	5468	0	119311	119310	-1
Aug-14	4620	4620	0	144632	144065	-567
Sep-14	4303	4303	0	134322	134260	-62
Oct-14	6037	6037	0	99404	99266	-138
Nov-14	4084	4084	0	106268	106225	-43
Dec-14	1528	1528	0	109459	109446	-13
Jan-15	2727	2727	0	80177	80177	0
Feb-15	3920	3920	0	80152	79957	-195
Mar-15	2112	2112	0	119445	118619	-826
Apr-15	3639	3639	0	91450	91229	-221
May-15	5590	5590	0	128383	127441	-942
Jun-15	3905	3905	0	132482	132401	-81
Jul-15	5087	5087	0	148861	148832	-29
Aug-15	2769	2769	0	139783	139630	-153
Sep-15	2691	2691	0	77581	77512	-69
Oct-15	6134	6134	0	92686	92475	-211
Nov-15	2216	2216	0	95848	95840	-8
	Total		0	Total		-5848

State of Art

- Services represent an important Inflow of money !

US Dollar thousand	Exported Services	Imported Services	EX-IM
2005	10,864,100	7,890,190	2,973,910
2006	11,672,800	8,730,540	2,942,260
2007	12,758,500	9,983,180	2,775,320
2008	17,635,600	13,458,700	4,176,900
2009	16,909,900	14,042,700	2,867,200
2010	16,040,100	13,034,000	3,006,100
2011	19,672,600	12,963,300	6,709,300
2012	14,615,900	11,444,900	3,171,000
2013	15,101,166	12,853,400	2,247,766
2014	13,761,000	12,521,100	1,239,900
total			32,109,656

State of Art

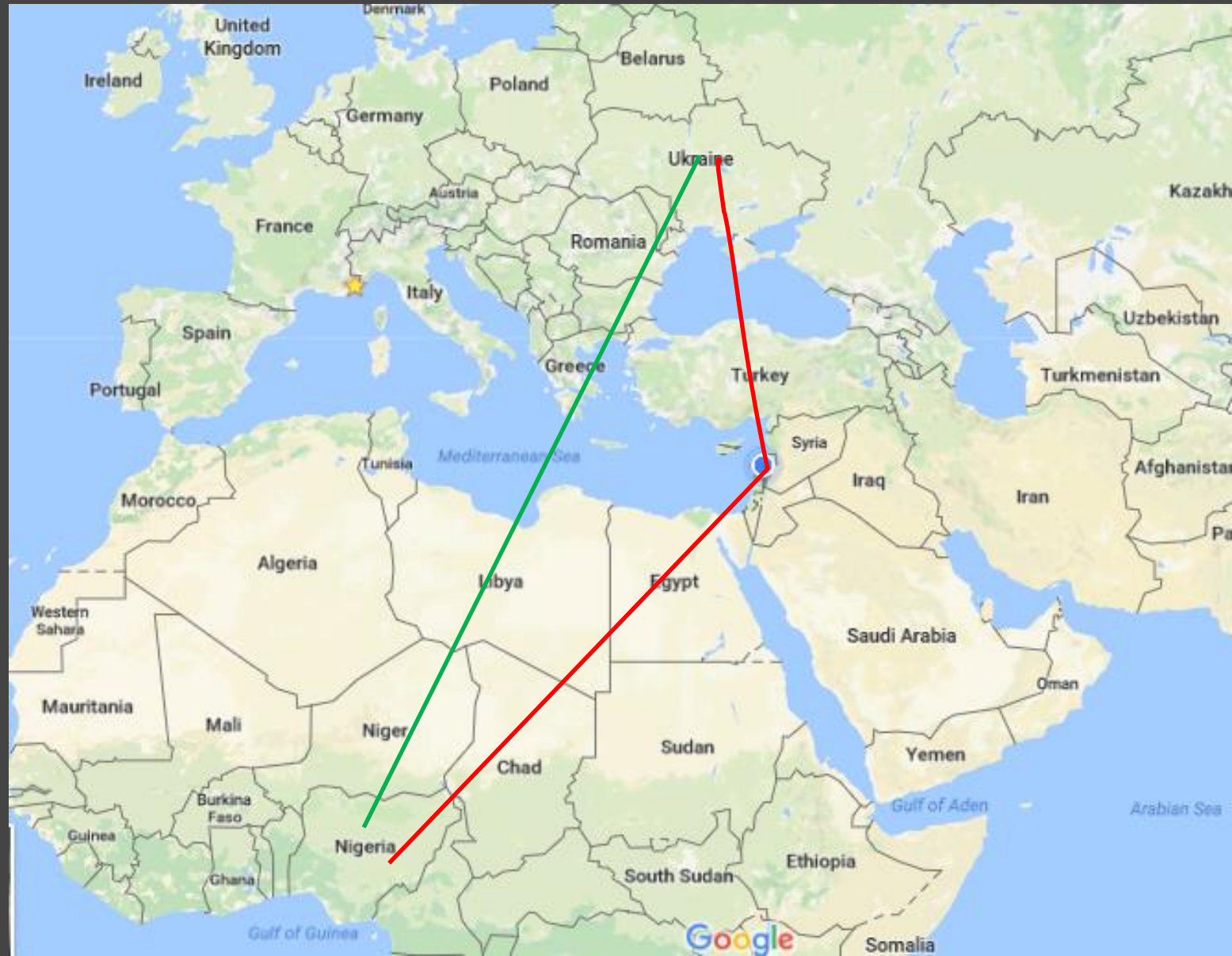
Code	Label	Imported value in 2012	Imported value in 2013	Imported value in 2014
S	All services	11444900	12853400	12521100
SOX	Memo item: Commercial services	11424921	12828208	12500879
4	Travel	4199450	4387750	4998640
10	Other business services	2671180	3901830	3171780
3	Transport	2233600	2280080	1939610
7	Financial services	594220	581195	1035200
9	Telecommunications, computer, and information services	548558	542673	433711
6	Insurance and pension services	428824	600025	308120
5	Construction	431810	270825	290064
11	Personal, cultural, and recreational services	276237	313327	283737
8	Charges for the use of intellectual property n.i.e.	32816	28121	34702
12	Government goods and services n.i.e.	19979	25192	20221
2	Maintenance and repair services n.i.e.	12785	11963	7593

State of Art

Code	Service label	Exported Value in 2012	Exported Value in 2013	Exported Value in 2014
S	All services	14615900	15101166	13761000
SOX	Memo item: Commercial services	14483531	15051300	13725462
4	Travel	6327480	5872360	6272250
10	Other business services	3564780	4702290	2963250
7	Financial services	1587630	1508720	1785210
3	Transport	1148430	1127570	976853
9	Telecommunications, computer, and information services	645904	595873	689491
5	Construction	589149	743244	629283
11	Personal, cultural, and recreational services	316499	228108	275494
6	Insurance and pension services	174444	185338	69856
1	Manufacturing services on physical inputs owned by others	114912		36896
12	Government goods and services n.i.e.	132369	49866	35538
8	Charges for the use of intellectual property n.i.e.	2659	75865	18367
2	Maintenance and repair services n.i.e.	11620	11932	8569

Analysis

- Services represents, by excellence, a source of IFF since we can't prove the effective execution of the business transaction
- Example: Lebanese offshore acting as an intermediary between an Ukrainian Wood Company and an African country



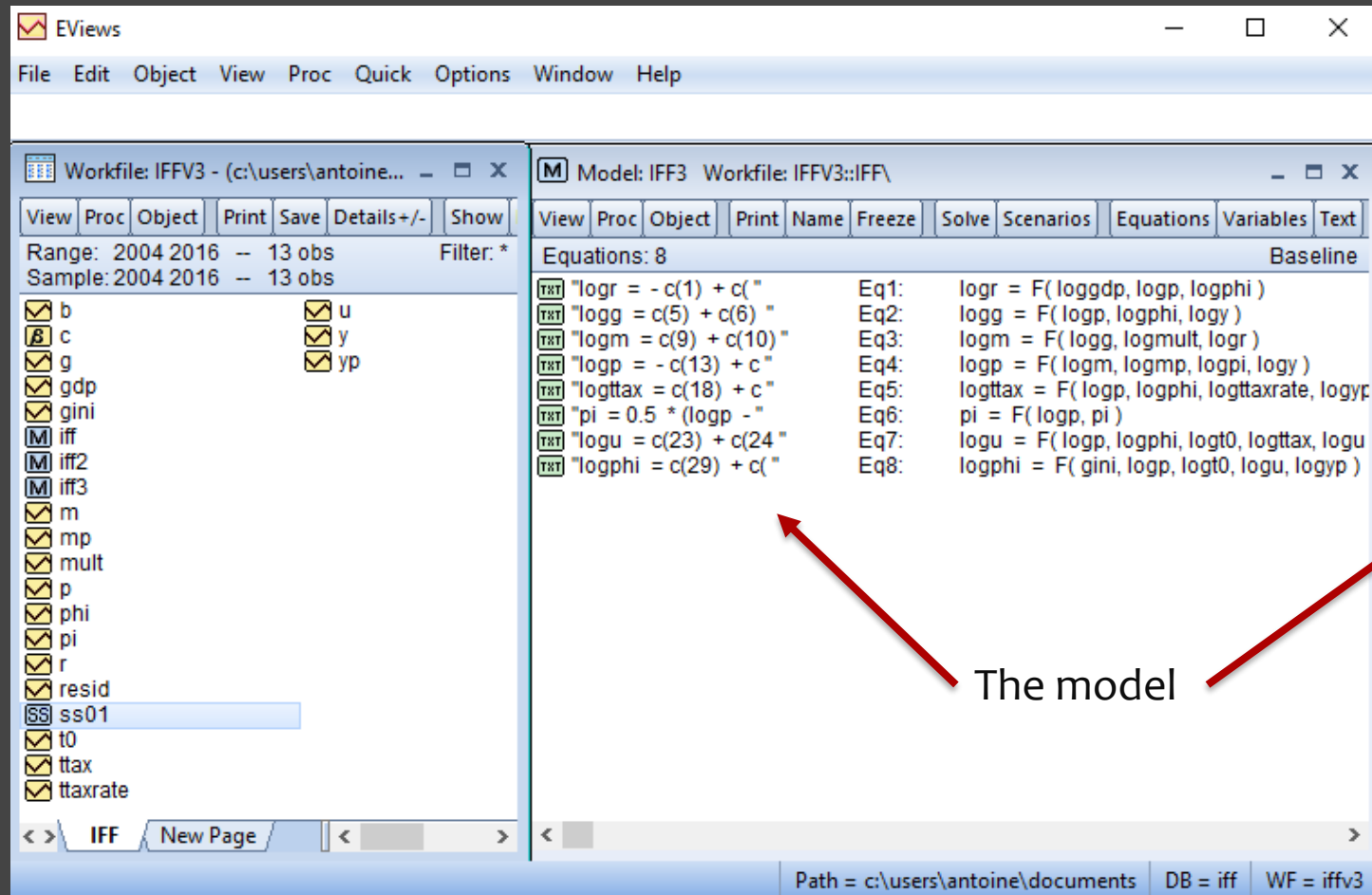
Analysis

- Main Vehicles for IFFs in Lebanon are:
 - Services,
 - Oil & Gas,
 - Vehicles,
 - pearls and precious metals,
 - Pharmaceutical products,
 - Electrical machines

Analysis

- Government Request for Proposal constitutes also a vehicle for outflow money from Lebanon to the bank account of the decision makers.
- The openness of the borders between Lebanon and Syria, leads to make from Lebanon a window for IFFs coming from and to Syria, Iraq and Turkey
- Corruption in Lebanon is a catalyzer for the IFFs
- ...

Analysis



Workfile: IFFV3 - (c:\users\antoine...)

Model: IFF3 Workfile: IFFV3::IFF\

Range: 2004 2016 -- 13 obs
Sample: 2004 2016 -- 13 obs

Filter: *

Variables:

- ☒ b
- ☒ c
- ☒ g
- ☒ gdp
- ☒ gini
- ☒ iff
- ☒ iff2
- ☒ iff3
- ☒ m
- ☒ mp
- ☒ mult
- ☒ p
- ☒ phi
- ☒ pi
- ☒ r
- ☒ resid
- ☒ ss01
- ☒ t0
- ☒ ttax
- ☒ ttaxrate
- ☒ u
- ☒ y
- ☒ yp

Equations: 8

Eq1:	Eq2:	Eq3:	Eq4:	Eq5:	Eq6:	Eq7:	Eq8:
logr = -c(1) + c(2)	logg = c(5) + c(6)	logm = c(9) + c(10)	logp = -c(13) + c(14)	logttax = c(18) + c(19)	pi = 0.5 * (logp - logp0)	logu = c(23) + c(24)	logphi = c(29) + c(30)
logr = F(loggdp, logp, logphi)	logg = F(logp, logphi, logy)	logm = F(logg, logmult, logr)	logp = F(logm, logmp, logpi, logy)	logttax = F(logp, logphi, logttaxrate, logyp)	pi = F(logp, pi)	logu = F(logp, logphi, logt0, logttax, logu)	logphi = F(gini, logp, logt0, logu, logyp)

The model

Government Revenues:

$$\log R_t = -a_0 + a_1 \log GDP_t + a_2 \log P_t + a_3 \log \psi_t$$

Government Expenditures:

$$\log G_t = b_0 + b_1 \log Y_t + b_2 \log P_t + b_3 \log \psi_t$$

Broad Money Supply:

$$\log M_t = k_0 + k_1 \log Mult_t + k_2 \log G_t - k_3 \log R_t + k_4 \log E_t$$

Price Level:

$$\log P_t = -c_0 + c_1 \log Y_t + c_2 \log \pi_t - c_3 \log (M/P)_{t-1} + c_4 \log M_t$$

Total Taxes Collected:

$$\log TTax_t = d_0 + d_1 \log \dot{Y}_t + d_2 \log TTaxrate_t + d_3 \log P_t + d_4 \log \psi_t$$

Expected Rate of Inflation:

$$\pi_t = \delta \Delta \log P_t + (1 - \delta) \pi_{t-1}$$

Underground Economy:

$$\log U_t = e_0 + e_1 \log P_t + e_2 \log \psi_t - e_3 \log TTax_t + e_4 \log U_{t-1} + e_5 \log TO_t$$

Illicit Outflows:

$$\log \psi_t = w_0 + w_1 \log P_t + w_2 \log U_t + w_3 Gini_t + w_4 \log \dot{Y}_t + w_5 \log TO_t$$

Analysis

- Marco-Econometric model to estimate the flow of IFFs: GFI book “Illicit Financial Flows: The Most Damaging Economic Condition Facing the Developing World”
- Data has been reconstructed (with considerable errors) from 1993-2016 using available data from different sources and spline interpolation for missing data
- Our estimation: with probability more than 95%. **IFFs represents more than 7% of the nominal GDP per year.**

Recommendations

- Establish a **unique database** within Lebanon between the customs, ministry of finance and ministry of economy and trade
- Establish a **national unit to coordinate actions against IFFs** and corruption and not subject to bank secrecy
- Establish **mandatory information exchange mechanism** inter-country between national IFFs fighting units
- Set a **new law** for making commercial transactions more transparent and **making the IFFs illegal and punished** by the Lebanese authorities

Recommendations

- Make all transactions with value greater than 3000 USD, electronically paid through checks, Credit Card or any other electronic payment
 - Set a specific law for multinational and offshore companies for better transparency
 - Enhance the role of customs
-
- Thanks for the ESCWA for raising this problem

